Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Applications by Qwest Communications,	)	
International Inc. for Authorization to	)	CC Docket No. 02-314
Provide In-Region, InterLATA Services	)	
in Colorado, Idaho, Iowa, Nebraska,	)	
North Dakota, Montana, Utah, Washington	)	
and Wyoming	)	

COMMENTS OF COVAD COMMUNICATIONS COMPANY

K. Megan Doberneck
Senior Counsel
mdoberne@covad.com

Praveen Goyal
Senior Counsel for Government
and Regulatory Affairs
pgoyal@covad.com

Jason D. Oxman
Assistant General Counsel
joxman@covad.com

Covad Communications Company
600 14th Street, N.W., Suite 750
Washington, D.C. 20005
202-220-0400 (voice)
202-220-0401 (fax)

Introduction

Covad is encouraged by Qwest's commitment in its latest 271 application filing to provide router testing for competitors' UNE line shared loops.[1] Covad continues to work cooperatively with Qwest to ensure that its rollout of router testing will truly provide competitors with non-discriminatory access to the same router testing Qwest employs for itself.[2] Covad remains optimistic that, during the course of its present 271 applications, Qwest will conclusively demonstrate that its line sharing provisioning processes for competitors, including its new router testing process, provide competitors with truly non-discriminatory access to UNE line shared loops.

Although Covad is encouraged by Qwest's commitment to providing router testing for CLEC line shared loops, Covad continues to believe that Qwest's pending applications exhibit serious defects, including Qwest's failure to establish that it provides competitors with non-discriminatory access to loop-makeup information, Qwest's failure to provide pre-order access to MLT testing for UNE loops, and, perhaps most significantly, Qwest's pricing for the line shared loop UNE.[3] Indeed, the single, most egregious ongoing deficiency in Qwest's pending applications is Qwest's pricing of line shared loops in Colorado and Washington. As detailed in Covad's previous filings

[1] *See* Addendum to Qwest Brief, section entitled "Status of Router Testing for Line Sharing" (filed September 30, 2002).

[2] For example, Qwest's roll-out of router testing for competitors should ensure that (a) competitors are not charged for Qwest's performance of router testing, because such testing is encompassed by Qwest's obligation to provide non-discriminatory access to a working loop; (b) that Qwest rolls out router testing for competitors whenever it rolls out router testing for itself in new central offices; and (c) that Qwest completes its implementation of router testing for competitors in a reasonably rapid time-frame and by a date certain no later than the end of 1Q 2003.

[3] *See* Covad Comments in WC Docket No. 02-148; Covad Reply Comments in WC Docket No. 02-148; Covad Comments in WC Docket No. 02-189; and Covad Reply Comments in WC Docket No. 02-189.

opposing Qwest's 271 applications, Qwest has clearly failed to meet its required burden of showing that its non-zero line shared loop rates in Colorado and Washington pass TELRIC muster. In these comments, Covad provides additional responses to Qwest's efforts at leading the Commission to ignore these serious gaps in Qwest's 271 showing. Thus, Covad continues to believe that Qwest has failed to make the requisite statutory showing required before Qwest can be granted interLATA section 271 authorization. Until these issues are resolved, Qwest's 271 applications cannot be granted.

Discussion

As discussed in detail in Covad's previous filings, Qwest's pricing for the UNE HFPL in the states of Colorado and Washington represents a clear violation of TELRIC.[4] Qwest has failed to provide an adequate response to Covad's demonstration that these rates constitute a clear, ongoing violation of the Commission's pricing rules and therefore section 271. Qwest must not be allowed into the interLATA market until it charges competitors the same price Qwest continues to charge itself: $0. This non-discriminatory price is the only method by which to remedy the *clear* violation of TELRIC perpetrated by Qwest's positive rates for the HFPL in Colorado and Washington respectively.

Qwest's attempts to rebut Covad's demonstration of Qwest's clear TELRIC violations amount to little more than obfuscation of the facts – and the law. Contrary to Qwest's characterization,[5] there is nothing unclear at all about the pricing principles for UNE line shared loops set forth by the Commission in its *Line Sharing Order*. To the

[4] *See* Covad Comments in WC Docket No. 02-148 at 5-13; Covad Reply Comments in WC Docket No. 02-148 at 2-8; Covad Comments in WC Docket No. 02-189 at 5-16; and Covad Reply Comments in WC Docket No. 02-189 at 2-11.

[5] *See, e.g.,* Qwest Reply Brief in WC Docket 02-189 at 102-103.

contrary, those principles could not be clearer: incumbent LECs should not charge competitors more for the UNE HFPL than the incremental loop costs they allocate to their own xDSL services.[6] Contrary to Qwest's vague reference to a "persistent debate" about these principles, in the three years since the Commission adopted them there has been no change in them whatsoever. Whatever "debate" there may be about them, these pricing principles remain in full effect. Contrary to Qwest's vague allusions, there simply is no dispute here that is "appropriately the subject[] of industry-wide notice-and-comment rulemaking."[7] The only dispute here is whether as a matter of fact Qwest has met its burden of showing that its line shared loop rates are based on TELRIC costs. As Covad has now repeatedly shown, they simply are not.

Furthermore, Qwest's allusion that the D.C. Circuit's *USTA v. FCC* decision somehow alters its current legal obligations with respect to line sharing or line sharing pricing is absurd.[8] Qwest knows full well that the court affirmed the FCC's judgment that the high frequency portion of the loop properly qualified as a discrete "network element," a critical cornerstone of the Commission's *Line Sharing Order* that has now withstood judicial review.[9] The Court's remand of the *Line Sharing Order* was merely premised on its opinion that the Commission failed to adequately consider cable modem competition in requiring the unbundling of the high-frequency portion of the loop. On remand, the Commission is therefore required to analyze the extent to which cable modem service effects impairment. None of this, however, alters the current

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[6] *Line Sharing Order*, ¶ 139.

[7] *See id.*

[8] *See id.*

[9] *USTA v. FCC,* 290 F.3d 415, at 429 (D.C. Cir. 2002).

effectiveness of the Commission's line sharing rules, nor of the Commission's ability to readopt them as is, consistent with the direction of the Court's opinion. In fact, the Court's recent stay of its vacatur of the *Line Sharing Order* was premised on the Commission's ability to continue to require the unbundling of line shared loops.[10] Thus, the continuing effect of the Commission's *Line Sharing Order*, including the pricing principles clearly set forth therein, is without question.

Furthermore, Qwest's misguided attempt at demonstrating its retail margins for line shared xDSL services in the states where it does charge positive HFPL rates fails to establish in any way that Qwest's line shared xDSL retail rates actually recover any loop cost. Qwest argues that because its retail margins for 2 retail xDSL service offerings in Washington would stand at 42% and 76% respectively <u>if</u> the UNE HFPL cost were also attributed to Qwest's xDSL costs, Qwest's retail rates must therefore have been designed to recover some loop cost which is at least as high as the UNE HFPL rate.[11] It takes an extraordinary leap of faith to believe that, as per Qwest's own characterization, an incumbent monopolist that designed retail rates with a 76% margin in mind could not have also easily designed retail rates with an 86%, 90% or 99% margin for that matter. Indeed, given that Qwest's retail xDSL rates are region-wide, what margins does Qwest enjoy in states where it has not been permitted to charge a positive HFPL rate? The fact

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[10] In its motion for a partial stay of the Court's vacatur, WorldCom argued that that the FCC could well re-adopt line sharing rules consistent with the Court's decision, and that it would be deeply disruptive to the status quo and to the thousands of customers benefiting from competitive services offered over line-shared loops if the line sharing rules were vacated pursuant to the Court's mandate, only to have those rules reinstated by the Commission in the Triennial Review. The Court agreed with these arguments, staying the mandate only until January 2003 based on the FCC's representations that by that time it will have adopted new line sharing rules as part of its Triennial Review Process. *See Order* dated September 4, 2002, citing *Triennial Review NPRM* ¶ 81 (FCC is currently reviewing rules for trinnial review that is to be completed in 2002).

[11] *See* Thompson Pricing Reply Declaration in WC Docket 02-189 at 35-36.

is that Qwest's so-called "imputation" analysis does nothing to show that its retail xDSL rates actually include any recovery for loop costs. More importantly, Qwest's analysis does nothing to show that its xDSL rates recover loop costs not already recovered elsewhere in Qwest's retail rates for basic voice services. Given that the rates and rate structure for Qwest's basic voice service rates were designed well before xDSL product offerings were brought to market, it strains credulity to believe that Qwest's retail basic voice service rates do not already fully recover its loop costs, even in the absence any xDSL service on the same line. Otherwise, Qwest would lose money on over 95% its consumer voice customers, who do not subscribe to xDSL.[12] Qwest's depiction of its incremental loop costs resulting from line shared xDSL simply strains credulity.

The fact is, as Covad has now repeatedly demonstrated, Qwest has failed to develop costs underlying its HFPL rates in Colorado and Washington in compliance with the Commission's TELRIC rules – indeed, the HFPL rate amounts appear to have been picked out of a hat. Qwest has failed to prove that it sustains any costs, much less TELRIC-compliant costs, through production of a TELRIC-compliant cost study, even though such a study is required by the FCC's pricing rules. Moreover, Qwest has failed to apply the pricing principles set forth by the FCC in the *Line Sharing Order* for the pricing of the HFPL. The FCC developed these pricing principles precisely to prevent incumbents from fully recovering loop costs prior to any offering of line shared xDSL service, while at the same time charging competitors for the use of the loop. In fact, Qwest has failed to show that the use of the high-frequency portion of the loop results in

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[12] *See* Qwest Communications Inc. Selected Consolidated Data for 2Q 2002, Attachment E (reporting 485,000 in-region DSL subscribers vs. over 11 million consumer access lines); available at http://media.corporate-ir.net/media_files/NYS/q/Q_Q2_02.htm.

any incremental loop costs whatsoever – and so Qwest seeks the imposition of an illegal "market-based" rate rather than a cost-based rate. Indeed, Qwest's positive rates for UNE HFPL in Colorado and Washington result in clear discrimination against competitors, artificially inflating competitors' costs of providing line shared xDSL services above Qwest's costs. Moreover, these rates result in double-recovery of loop costs by Qwest. Even after multiple rounds of 271 filings before this Commission, Qwest has provided no evidence to counter these facts.

Qwest has falsely argued to this Commission that UNE HFPL pricing is somehow exempt from the FCC's TELRIC pricing standard.[13] As Covad has shown, however, UNE HFPL pricing must conform to the same TELRIC pricing standard this Commission requires for all UNEs. Indeed, the FCC's *Line Sharing Order* provided a simple prescription for setting UNE HFPL prices utilizing TELRIC principles: incumbent LECs should not charge competitors more for the UNE HFPL than the incremental loop costs they allocate to their own xDSL services.[14] The FCC took pains to make clear that this HFPL pricing principle was fully consistent with TELRIC:

> These guidelines either follow directly from the … TELRIC … methodology that the Commission set forth in the *Local Competition First Report and Order* to govern interconnection and unbundled network element pricing, or, if not a direct outgrowth of those principles, are consistent with them in the context of this particular unbundled network element.[15]

[13] *See*, *e.g.,* Declaration of Jerrold Thompson, Qwest Opening Brief in WC Docket No. 02-148, at p. 69, para. 106 (falsely stating that the FCC's Line Sharing Order, "instead of using TELRIC," sets forth permissive, non-TELRIC pricing principles for UNE HFPL).

[14] *Line Sharing Order*, ¶ 139 (emphasis added).

[15] *Line Sharing Order*, ¶ 132.

Notwithstanding the FCC's clear direction on how states should develop pricing for UNE HFPL in conformance with TELRIC pricing principles, the state commissions in Colorado and Washington decided that they would diverge from the pricing principles set forth in the *Line Sharing Order*, and decided to impose a positive rate in excess of the zero loop costs Qwest allocates to its tariffed xDSL service. In fact, the Washington Utilities and Transportation Commission, quoting testimony from Qwest's own witness, takes note of the fact that Qwest treats its tariffed line shared xDSL service as causing no incremental loop costs.[16] During the Washington cost proceedings, Qwest reaffirmed that it incurs no direct or incremental loop costs when providing the HFPL:

> Q: Now, focusing again on what we have described as the loop, the piece of copper between the network interface device and the central office, isn't it correct that there are no additional costs to the loop itself when a CLEC provides DSL service using the HUNE?
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> A: That's correct … [T]here are not any additional costs.[17]

Qwest even went so far as to explain that: "In the retail service environment for [Qwest DSL] service, the cost of the loop is attributed to basic service, and therefore there is no incremental cost of the loop attributed to [Qwest DSL]."[18] The Washington Commission proceeded, nonetheless, to set an arbitrary price of $4 for the UNE HFPL, operating under the mistaken assumption that some positive rate must be required, and that a $4

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[16] *Washington Utilities and Transportation Commission, Continued Pricing of Unbundled Network Elements, Transport and Termination,* 13th Supplemental Cost Order, Part A, Docket No. UT-003013, at 14.

[17] WA Cost Hearing Trans., (Fitzsimmons), pp. 181:3-11; *see also* WA Cost Hearing Ex. 11 (Thompson Supp. Direct), pp. 5-6; WA Cost Hearing Ex. 194 (Cabe Response), p. 3; WA Cost Hearing Ex. 350 (Spinks Direct), p. 12.

[18] WA Cost Hearing Ex. 34 (Qwest response to Covad Data Request 01-021); *Line Sharing Order*, ¶¶ 41 and 55.

rate does not create a price squeeze. As long as Qwest admits that there are no incremental loop costs in providing line shared xDSL service, however, no positive rate for competitors can pass TELRIC muster.

Furthermore, as long as Qwest fully recovers its loop costs prior to any line shared xDSL being offered, but competitors must nonetheless pay positive HFPL loop rates when they provide line shared xDSL service, competitors' costs will always be inflated artificially above Qwest's costs for the same service. This is precisely the kind of discriminatory "price squeeze" the *Line Sharing Order*'s TELRIC pricing principles for UNE HFPL sought to prevent:

> This approach also helps alleviate any potential price squeeze… By requiring incumbent LECs to provide access to the shared local loops for no more than they allocate to their own xDSL services, the price squeeze may be redressed by ensuring competitive LECs and ILECs incur the same cost for access to the bandwidth required to provide xDSL services.[19]

The fact that the rate for UNE HFPL in Washington state has been reduced from $4 to $2 thus simply reduces the amount of the price squeeze. Yet this rate reduction does nothing to eliminate the type of price squeeze that was the central focus of the Commission's concern in its *Line Sharing Order*.

Covad disputes the notion that the HFPL should be priced as a positive allocation of shared loop costs, because Covad believes that use of the high frequency portion of the loop results in no incremental loop costs – in apparent agreement with Qwest, as evidenced by the loop cost allocation for its retail xDSL service, and by its own testimony. The fact is that Qwest admitted in another proceeding that the loop should not be viewed as a shared cost:

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[19] *Line Sharing Order*, 14 FCC Rcd 20912, at para. 141.

> Economists generally disagree with the view that the local loop is shared facility because it conflicts with the fundamental principle of cost causation, which, in economics, attributes a cost to the source (an economic decision or activity) that gave rise to it. According to this principle, the costs associated with the loop are caused by a customer gaining access to the network.
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> ***
>
> The contrary position that the loop's cost should depend on how it is used is based on a fallacy that confuses the cost causer (namely, the consumer or purchaser of the loop) with the entity that incurs and feeds to recover the cost (namely, the supplier of the loop).
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> ***
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> ***Question: Do you accept the premise that the local loop is a shared facility whose costs should be allocated to different services? Answer: No. This premise is contrary to sound economic principles and based on an incorrect approach to cost recovery processes***.[20]

In an *ex parte* letter, Qwest provides little more than a feeble attempt to explain away this testimony.[21] Qwest's *ex parte* fails to explain why it makes sense for Qwest to apply the cost allocation principles set forth in its testimony to loop cost allocation among Qwest services, but not for competitors to apply the same cost allocation principles to loop cost allocation among UNEs. Either the cost for a facility should be allocated entirely to the source of the activity giving rise to the need for that facility, as Qwest's testimony indicates, or not. In other words, either loop costs should be allocated entirely to "a customer gaining access to the network" via basic voice services, as per Qwest's testimony – and not at all to the UNE HFPL used to provide line shared xDSL alongside

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[20] WA Cost Hearing Trans. (Fitzsimmons), pp. 241-43.

[21] *See* Letter from David Sieradzki, Hogan and Harston, to Marlene Dortch, FCC, filed August 15, 2002 in WC Docket 02-189, at 14.

existing voice services[22] – or they should not. Qwest is speaking out of both sides of its mouth when it states that the cost allocation principle reflected in its testimony is meant to apply only to pricing services, and not to pricing UNEs. Indeed, the cynical view would be that Qwest pays lip service to this cost allocation principle when it serves to maximize Qwest's revenue (from rate-of-return local rates, as opposed to price-capped exchange access rates), but then refuses to be held to the same principle when it would decrease Qwest's revenues from UNE HFPL.

Nevertheless, even assuming *arguendo* that UNE HFPL should be priced as an allocation of shared loop costs, Qwest has failed to meet the evidentiary burden of showing the positive rates it charges in Colorado and Washington are TELRIC-compliant. This is the case because Qwest failed to produce a cost study supporting these rates. The fact is that Qwest never even attempted to show that it incurs costs in providing the HFPL, and never developed a cost study containing a methodology for allocating loop costs as a common cost. That is, Qwest never provided a cost study supporting its claimed HFPL costs. Standing alone, this failure too demonstrates a clear violation of TELRIC. The FCC has made clear that the *only* method by which an incumbent LEC may prove that its rates are *cost-based* and compliant with FCC pricing rules is through a *cost study*:

> (e) Cost study requirements. An incumbent LEC *must prove* to the state commission that the rates for each element it offers do not exceed the forward-looking economic cost per unit of providing the element, *using a cost study that complies with the methodology set forth in this section and* § *51.511*. 47 C.F.R. § 51.505(e) (emphasis added).

[22] Covad notes that the rules defining line shared loops only permit the high-frequency portion of the loop to be unbundled if incumbent-provided voice service is also present on the loop. *See* 47 C.F.R. § 51.319(h)(3).

As the FCC further specified in the body of its pricing rules, a cost study sufficient to support a claim of cost-based pricing must include support for the joint or common costs associated with the UNE at issue:

> Cost studies must include the forward-looking cost over the long run of the total quantity of the facilities and functions that are directly attributable to, or reasonably identifiable as incremental to, such elements . . . measured based on the use of the most efficient telecommunications technology currently available and the lowest cost network configuration *[plus a] reasonable allocation of forward-looking common costs*. . . . 47 C.F.R. § 51.505.

Equally fatal to Qwest's desire to charge a positive HFPL rate are the problems associated with double recovery. While Qwest has indicated that it will deaverage HFPL rates in some states, deaveraging a positive rate does nothing to address the fact that a positive rate results in double-recovery in the first place. In sum, Qwest's positive HFPL rate is not accompanied by any commitment to rebalance Qwest's rates for other services that already fully recover its loop costs. In the absence of such rebalancing, as the Department of Justice acknowledged in its Comments on the ROC I applications, Qwest will over-recover the cost it incurs in provisioning line shared loops since it already recovers all of its loop costs through rates for other services. That is, Qwest will recover more than its costs, in violation of TELRIC, since it already recovers all of its loop costs prior to any line shared xDSL service being offered, and then will receive additional income from the HFPL rates.

Qwest's response to the problems of double-recovery created by its positive HFPL rates is its *ex parte* statement that Qwest's "local exchange rates" do not fully recover its loop costs.[23] This argument is an extraordinary red herring. First, Qwest itself

[23] *See* Letter from David Sieradzki, Hogan and Harston, to Marlene Dortch, FCC, filed August 15, 2002 in WC Docket 02-189, at 13.

admitted that it is subject to rate-of-return regulation in Washington state, guaranteeing Qwest complete recovery of its plant costs, including its loop costs, for the provision of basic local services.[24] Second, any recovery of loop costs outside of local exchange rates (such as from the interstate subscriber line charge) does nothing to alleviate the double-recovery created by a positive HFPL rate. Qwest does not argue that its current rate structure for basic services results in under-recovery of its loop costs, nor could it support such an assertion. The fact is that, as evidenced by Qwest's own allocation of zero loop costs to its line shared xDSL services, Qwest fully recovers its loop costs prior to offering any line shared xDSL services. Consequently, any positive HFPL rate for competitors results in over-recovery of loop costs by Qwest.

Qwest also argues that its 271 application is not the appropriate forum in which to examine this double-recovery of its loop costs from competitors.[25] The sheer audacity of this argument is stunning. Qwest asks for the Commission to ignore its anticompetitive and discriminatory HFPL pricing, which clearly runs afoul of the Commission's pricing principles established in the *Line Sharing Order*, in the very proceeding intended by Congress to examine whether Qwest's local markets are open to competitors like Covad. Qwest asks the Commission to ignore its discriminatory UNE pricing, in the very proceeding meant to determine whether Qwest's UNE pricing is cost-based and TELRIC-compliant before allowing it to vertically enter interLATA markets. Moreover, Qwest

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[24] WA Cost Hearing Ex. 350 (Spinks Direct), p. 12. In Washington, Qwest is subject to rate of return regulation pursuant to which Qwest fully recovers its loop costs for basic voice services. *See* WA Cost Hearing Trans. (Thompson), p. 536:1-537:21. Further, Qwest publicly pledged in May 2000 that it would not increase its tariffed voice rates, despite the probability of a zero HFPL.

[25] *See* Letter from David Sieradzki, Hogan and Harston, to Marlene Dortch, FCC, filed August 15, 2002 in WC Docket 02-189, at 13.

asks that the Commission allow it into the interLATA voice and data marketplace, while it continues to over-recover its loop costs from competitors like Covad, and in the meantime leave off to a future, unspecified date any removal of costs from its local rates, in unspecified proceedings that have yet to be initiated. Qwest's position leaves no guarantee that any such future proceeding would in fact appropriately remove from basic service rates the loop costs Qwest now recovers from competitors in UNE HFPL rates – leaving aside for the moment that Qwest has failed to show with a cost study that the positive rates it currently recovers even comply with TELRIC! Indeed, Qwest's position leaves no guarantee that any future rate rebalancing proceedings would in fact occur. Qwest further fails to mention that it has every incentive to continue allocating as much loop cost as it can to basic voice services, for which it remains the dominant provider.[26] Qwest wants the Commission to give Qwest its 271 cake now, and count on Qwest not to eat it later. Qwest is essentially asking for the Commission to perpetuate indefinitely an untenably anticompetitive situation, and provide Qwest with 271 authority to boot. The audacity of this argument is outrageous.

Qwest's pricing of the HFPL in Colorado and Washington represents a clear violation of TELRIC and Section 271(c)(2)(B)(i). Qwest's applications for Section 271 relief must be rejected until it sets the HFPL at $0 in both states.

[26] Indeed, the other BOCs routinely allocate as much loop cost to their non-xDSL services and as little to their retail xDSL services as they can. For example, Verizon, which discloses no loop costs for its federal DSL retail service, has voluntarily proposed a $0 rate for the HFPL. Similarly, SBC, which also discloses no costs for its retail DSL product, has a $0 HFPL rate in Illinois, Kansas, Michigan and Texas. BellSouth, region-wide, has an HFPL MRC of just over $0.50. Given this context, Qwest's $4 rate should stand out as a red flag to the Commission.

Conclusion

For the reasons stated herein and in Covad's previous filings, the Commission should reject the applications of Qwest for authority to provide in-region, interLATA services in Colorado, Idaho, Iowa, Nebraska, North Dakota, Montana, Utah, Washington and Wyoming.

Respectfully submitted,

/s/ Praveen Goyal

Megan Doberneck
Senior Counsel

Jason Oxman
Assistant General Counsel

Praveen Goyal
Senior Counsel for Government
and Regulatory Affairs

Covad Communications Company
600 14th Street, N.W.
Washington, D.C. 20005
202-220-0400 (voice)
202-220-0401 (fax)

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